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C O N F I D E N T I A L SECTION 01 OF 02 BRUSSELS 002938

SIPDIS

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TAGS: [PREL](#) [EAID](#) [ETRD](#) [PGOV](#) [CY](#) [GR](#) [TU](#) [EUN](#) [USEU](#) [BRUSSELS](#)

SUBJECT: NEW COMMISSION PROPOSALS FOR NORTHERN CYPRUS

REF: A. USEU BRUSSELS 01870

[1](#)B. NICOSIA 01288

Classified By: Rick Holtzapple, PolOff, Reasons 1.4 (B/D)

SUMMARY

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[1](#)1. (SBU) On July 7, EU Enlargement Commissioner Gunter Verheugen presented the Commission's plan fulfill the EU's pledge to end the isolation of the Turkish Cypriot community following their support for the Annan Plan. The two main proposals are: 1) a new "preferential trade regime" allowing direct trade between northern Cyprus and EU Member States, including the rest of Cyprus; and 2) an EU aid package of 259 million euros to be spent in the North and dedicated primarily to infrastructure development and alignment with EU legislation and policies. Verheugen emphasized the political significance of the package, and acknowledged that the EU has a special obligation to Turkish Cyprus following its approval of the UN reunification plan, which was rejected by the South. In discussions with us, Commission officials have said this package represents all that the Commission can do for the north.

[1](#)2. (U) Summary (continued): The aid package should win unanimous Council backing, although the means of delivering the aid has still to be sorted out. The trade package is more controversial, as Commissioner Verheugen is attempting to use a qualified majority vote (QMV) procedure which neutralizes the influence of Cyprus and Greece on the package. For this reason the trade proposals are already facing stiff opposition from the Greek Cypriots and from Greece itself, who argue, despite Verheugen's assurances to the contrary, that direct trade with the North will entail the tacit recognition of Turkish authorities. Nicosia has indicated considerable dissatisfaction with Verheugen's QMV-based approach, and has expressed its determination to oppose the trade proposals in the European Court of Justice (ECJ). END SUMMARY.

PREFERENTIAL TRADE REGIME

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[1](#)3. (U) The Commission's proposal would establish direct trade between Turkish Cyprus and the EU under a preferential regime. The Commission says that this "should take the form of a tariff quota system." Goods originating in Northern Cyprus would have to be labeled as such, and measures would be in place to prevent what the Commission calls "artificial trade patterns" (i.e., transshipped goods from Turkey). Responsibility for this and for regulating exports in general would rest with the Turkish Cypriot Chamber of Commerce. Additionally, the Commission proposal sets rules on taxation, food and product safety, inspections, and communication obligations, which the Turkish Cypriots would have to abide by. Finally, the Commission would allow ports of Northern Cyprus, for the first time since 1974, to reopen to commercial traffic with the EU.

SUBSTANTIAL AID PACKAGE

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[1](#)4. (SBU) The Commission has proposed a total package of 259 million euros for 2004-2006, and the Council has previously approved this figure. The Commission says the money will be directed towards aligning Turkish areas with EU regulations and law, programs to improve contacts between the North and the South, social and economic developments, and infrastructure improvements. Verheugen singled out water treatment, tourism, agriculture, and small and medium sized enterprises as special areas of interest.

APPROVAL LIKELY, BUT IT'S NEVER EASY

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[1](#)5. (SBU) The Council is likely to approve the Commission's aid package, and the money should begin flowing into northern Cyprus in the near future. The idea of providing aid is accepted by all in principle. The real question is the degree to which Nicosia will seek to influence allocation decisions and methods. Notably, Verheugen said the Commission had not decided which delivery mechanism to use. This is significant because the method of distribution promises to be a source of debate in the Council, as it was last time the

Commission's aid proposal was discussed (REF A). The Commission wants to be able to disburse the funds independent of the Cyprus government in Nicosia, while the latter wants a hand in deciding how the money will be spent. Whether or not the EU will open a liaison office in the North remains an open question. A member of Commissioner Patten's cabinet told us that the two most serious options under consideration are either an "ad hoc" agency with an office in northern Cyprus, or administering the aid via the European Agency for Reconstruction based in Thessaloniki, which currently runs Commission aid programs for Kosovo, Serbia and Montenegro, and Macedonia. Cyprus is concerned that a EU liaison office would imply tacit recognition of the Turkish Cypriot authorities. While the Council (and therefore the Cypriot government) will have a say in this decision, the Commission expects to be able to implement whichever course it chooses.

16. (SBU) The Commission's trade proposal is even more controversial. Verheugen's decision to use Article 133 of the EU's treaties as the "legal basis" for the package -- which specifies that trade agreements with non-EU states are to be approved by qualified majority voting in the Council -- means that the measures should be easily passed in Council. But it is a highly contentious approach for Cyprus and Greece, who argue that Article 133 cannot be used for a territory that is legally part of the EU. The Greek Cypriots have voiced their determination to challenge the Commission at the ECJ; and it is by no means certain that the Commission's proposed regulation would survive the court challenge. Our Commission contact pointed out, however, that the new trade arrangement should remain in effect while an ECJ ruling is pending, and the ECJ "generally takes years to decide cases." He also noted that Greek Cypriot motivations for their legal arguments about the applicability of Article 133 are transparent, since Nicosia would almost certainly block the trade package under a consensus procedure, unless the key element -- the opening of direct trade between the north and the rest of the EU -- were withdrawn.

#### IMPACT ON TURKISH CANDIDACY

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17. (C) Our Commission contact noted that there was now overwhelming pessimism within the EU regarding the prospects for progress toward a Cyprus settlement prior to the EU Summit's decision in December on whether to open accession negotiations with Turkey. But he did not expect a continued division of Cyprus to be an obstacle to a favorable decision, for all but Nicosia. (NOTE: As Ref B explains, a settlement on Cyprus is a distinct issue from whether Turkey is treating the Republic of Cyprus, a full EU member, in a non-discriminatory manner. On that question, we agree with Embassy Nicosia's assessment that Nicosia's legal arguments enjoy broad EU support. End Note.) While he noted that Greek PM Karamanlis had "not been doing much to stand up to" the Greek Cypriots, Athens was expected to be generally supportive of Turkey's candidacy. But there was far less certainty about what Cypriot President Papadopoulos might do. Most worrisome to him was that it appeared there would be no domestic political price for Papadopoulos to pay if he blocked Turkey solely on the basis of a lack of a reunification agreement for the island. It would lead to the risk of a Cypriot government isolated within the EU, but stronger at home.

#### COMMENT

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18. (SBU) From our discussions with EU officials and the press reports coming out of Brussels, it is clear that the Cyprus government's intransigence over the Commission proposals continues to raise hackles in the Commission. While Turkish Cypriot authorities continue to benefit from post-referendum good will in Brussels, the reality of EU institutional functioning limits the ability of the Commission to play a strong hand in attempting to reward them for their yes vote on the Annan plan. The Commission is hoping to proceed as quickly as possible to improve economic conditions for the people of the north, despite fierce resistance from Nicosia. But the Commission is probably at the limit of what it will be able to do. It may even prove to be beyond that limit; while Verheugen's effort to channel trade through QMV is clever strategy, it is not clear that it will in the end be able to survive a challenge at the ECJ.

MCKINLEY